

SEATTLE CITY LIGHT:
PROTECTING THE JEWEL IN THE CITY'S CROWN

Final Report of the
MAYOR'S CITY LIGHT REVIEW COMMITTEE

Seattle, Washington

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Background

This year marks the 100th year of Seattle City Light and its distinguished history of providing reliable, low-cost electric power to the people of Seattle and surrounding communities. What began as a novel idea – public ownership and management of an electric utility – today stands as a model of public enterprise. For City Light is more than a business. This utility represents the reality that a community can own and successfully operate an electric power business and do so in a fiscally responsible and environmentally ethical manner.

City's Light's founders considered access to electricity an important and democratizing social goal. As physical access to electricity became universal, City Light's social policies have focused more on economic access through affordable electric rates for individuals and businesses. City Light's rates today remain among the lowest in the nation. Rates are set to recover only the cost of providing power, while ensuring the utility remains financially stable. In recent years, Seattle's elected officials have added energy conservation and environmental stewardship to the core of values driving City Light's business decisions.

Like many other developments in Seattle's history, the move to public ownership of the electric utility began with the Great Fire of 1889, when the City's private water system failed to provide firefighters with adequate water to battle the flames. Dissatisfaction with the private water utility during the fire led legendary City Engineer R. H. Thompson to persuade city officials to buy out the private owners and establish a municipally owned water utility.

One of the new water department's first projects was construction of a 37-mile pipeline from the Cedar River to Volunteer Park atop Seattle's Capitol Hill. In 1902, Seattle voters approved a bond issue to construct a hydroelectric plant on the Cedar River. It was the nation's first municipally owned hydroelectric project.

Thompson hired J.D. Ross as his assistant in charge of the hydroelectric project. Cedar Falls first generated power in 1905 under control of the City Water Department. The plant performed so well, and demand for municipal power rose so dramatically, the Seattle City Council soon decided to create a separate lighting department. On April 1, 1910, Seattle City Light was born and Ross became its first Superintendent. From this humble beginning grew today's impressive system of hydroelectric generation dams, transmission grid, and retail distribution assets.

Once the Cedar River hydroelectric plant was completed in 1905, it was followed by construction of the three hydroelectric power dams on the Skagit River, including Gorge (1924), Diablo (1930), and Ross (1940). In 1967, City Light

completed Boundary Dam on the Pend Oreille River in the northeastern corner of Washington.

The idea of local control has been a powerful element in the development of Seattle City Light. Throughout the utility's history, there has been a practice of going it alone. When the dams on the Skagit River were built, a risky and complex activity, there initially were no customers for them. Instead, customers had to be lured away from private utilities. Mayor Edwards, who proposed selling City Light and who fired J.D. Ross, was promptly recalled by voters in a special election, and the new Mayor, Robert Harlin, reinstalled Ross in charge of the utility.

This reaffirmation of faith in, and support for, City Light by the citizens of Seattle elevated the utility to a pedestal of high esteem in the community. The utility became untouchable even after Ross' death in 1939, a month after the first concrete was poured for Ruby Dam, now known as Ross Dam.

After World War II, the public/private power battle continued to be an ever-present feature of city politics. Customers were still served by two utilities, each with its own set of power lines, one private, and the other public. Then in 1951, by just over 900 votes, Seattle voters approved the buyout of Puget Power assets within the city limits.

The utility continued its "go-it-alone" philosophy and in 1967 developed a new project on the Pend Oreille River – Boundary Dam – that would more than double the utility's generation capacity.

Newly-elected Mayor Wes Uhlman came to City Hall in 1969, followed by a new, young, and aggressive City Council majority that had run on a progressive slate – Choose an Effective City Council (CHECC). This Council embraced some new ideas, such as beautification of the neighborhoods by undergrounding power lines, increasing minority representation in the City Light work force, new rate-making policies, and other items not high on the traditional City Light agenda. A second important development that year was passage of a new state budget law that granted the Mayor new executive budget authority. Now the City Council had to share with the Mayor as an equal the decisions on how to budget city revenues, including those at City Light. The Mayor now prepared the budget, not the chair of the Council's Finance Committee.

During the mid-1970's, City Light, with support from Mayor Uhlman, proposed the utility purchase shares in nuclear power plants 4 and 5, to be built by the Washington Public Power Supply System (WPPSS). Following a protracted and at times contentious debate, the Council rejected the WPPSS buy-in. Instead, through the policies adopted as part of its Energy 1990 study, the City Council enacted a new program in which City Light would first look to cost-effective energy conservation as the source of power to meet growing demands for

electricity. The City Council also authorized increasing the height of Ross Dam as another way to obtain additional electricity during periods of peak demand.

The Energy 1990 study produced more than a shift in policy. Between 1976 and 2001, City Light's nationally acclaimed (and often copied) conservation programs saved more than 6.5 million megawatt hours of electricity. The study also ushered in an era of citizen involvement on many levels that would last for years. The days of City Light as an impregnable citadel of utility independence were over. The specialists at the utility, who once had broad authority, now shared it with an active and informed City Council and a host of citizen committees engaged in designing new rates, conservation programs and policies, and environmental initiatives.

By the late 1980s, however, energy issues fell off the front page after the shock of the WPPSS bond default had swept through the region. Rates remained relatively low and City Light appeared to be relatively stable until the deregulation boom of the 1990's.

The following summarizes key features of Seattle City Light:

- The utility owns nearly 1,900 megawatts of very low cost, environmentally responsible hydroelectric generation capacity.
- City Light owns or contracts for about 60 percent of its own hydroelectric generating needs, and contracts for the remainder primarily through the Bonneville Power Administration.
- Now the nation's seventh largest publicly owned electric utility in terms of customers served, City Light provides its customers the lowest electric rates of the 25 most populous cities in the United States.
- City Light provides the City of Seattle general fund with \$30,000,000 in taxes.
- City Light's service area of 131.3 square miles includes the City of Seattle and the area north to the King County boundary (including the City of Shoreline and parts of Lake Forest Park), and extends south into the cities of Burien, Tukwila, and SeaTac.
- City Light's roughly 1,700 full-time employees serve more than 345,000 customers and a population exceeding 680,000.
- The utility's annual budget exceeds \$900 million.

Regulatory and Market Uncertainties

Changing market and political forces, as well as regulatory uncertainties, have seriously clouded the ability of City Light to plan for the long-term needs of its customers. From about 1992 to the present, Congress has annually debated

legislation that would provide greater competition in wholesale and, potentially, retail electric markets. The Federal Energy Regulatory Commission (FERC) has pursued a similar strategy. Many of the restructuring proposals contemplate a fully competitive wholesale market, with privately owned “merchant” generation, regional management of all transmission assets, and a residual distribution system role for existing electric utilities.

During 1996-1999, this approach to utility restructuring was implemented in 17 states, including the bellwether state of California. Many parties called for a uniform approach that would require either federal legislation or independent action by FERC.

This environment vastly complicates the traditional responsibility of electric utilities to meet all foreseeable needs of their firm retail customers. Typically, a utility will finance major investments in future generation with projected revenues from long-term power sales contracts. If the customers of those contracts are able to move to different providers, such financing becomes difficult, if not impossible. The tendency of utilities – both public and private – to avoid the risks of being short will be replaced by the opposite strategy of reducing long term resource investments.

For decades, the West Coast enjoyed relative price stability. For example, from May 1996 through May 1998, the average daily price at the Mid-Columbia trading hub was \$16 per megawatt hour, and the maximum was \$47. That changed dramatically when California’s power exchange began to operate in early 1998. From that point on, prices became more volatile, especially during the summer air conditioning season in California. Between May 1998 and April 2000, while the average price had barely changed, the maximum had increased to \$89. Then, beginning in May of 2000, the market became chaotic. Over the next 12 months, daily prices at Mid-Columbia averaged \$215 per megawatt hour and peaked at \$3,100. Hourly peaks hit \$7,000 per megawatt hour.

The West Coast power crisis of 2000-2001 revealed the horrible risks of being short. City Light paid more than \$600 million for wholesale power to meet firm retail needs during the winter of 2000-2001, at least an order of magnitude more than the utility expected to pay in a drought year. In response, City Light – and many other western public and private utilities – has rebuilt their power supply portfolios, afraid of market exposure if a similar crisis materializes.

Of concern to City Light is the threat of further restructuring, primarily from FERC initiatives. Despite the failure of the restructuring in California, FERC continues to press its agenda of market-driven prices at both the wholesale and retail levels. In a Notice of Proposed Rulemaking issued in July 2002, FERC detailed a plan to create five regional transmission authorities to manage the entire transmission system of the country. These entities, with the authority to dictate

resource acquisition to regions, would report directly to FERC, thus bypassing much of the traditional state and local control over electric utilities.

In this proposal, load-serving utilities like City Light would compete for scarce transmission capacity with power marketers. The market model FERC envisions, embodied in its Regional Transmission Organization (RTO) and standard market design rule making presents challenges and threats to the northwest, especially to its hydro-based generation system. Some fear the proposed pricing mechanism may be open to the kinds of market manipulation experienced in California during the recent energy crisis. The FERC's rules could be finished as early as December 2002, with implementation taking place over the next 18 months.

As of this writing, Congress is considering legislation that would subject transmission systems of publicly owned electric utilities such as Seattle City Light to greater FERC regulatory control. This, in turn, would increase the likelihood that FERC would require City Light to join an RTO, further eroding the authority of locally elected officials.

It is too early for us to conclude whether these rules could damage the portfolio decisions made by Seattle City Light in 2001. Clearly, the rules indicate the restructuring debate is not over, and there are continuing risks for resource investments in new generation, new transmission, and conservation.

Seattle City Light Governance

Seattle's municipal government embodies a strong Mayor/strong Council form of government, in which the Mayor and City Council share authority in a system of checks and balances as enumerated in the City Charter. This resembles the federal system of checks and balances, through which the President and Congress share governance responsibility for the nation. The Mayor manages department staff, including the hiring and firing of the department heads (subject to City Council confirmation), and day-to-day operations of the City. The Mayor also proposes a balanced budget to the Council each year. In turn, the Council reviews the Mayor's proposed budget, amends it as it sees fit, and then adopts it.

The City Council exerts its influence primarily through enacting legislation, approving a balanced budget, and confirming the Mayor's appointments of department heads (including the Superintendent of City Light). Relative to City Light, the Council's fiscal authority also includes the setting of electric rates, approval of borrowing, and approval of major investments in long-term contracts or licenses (for example, power contracts longer than 18 months). The City Council also retains authority over approval of property transfers, leases, or sales from the utility, and any major project initiatives (for instance, purchase of a power plant or acceptance of a FERC license). City Light also must obtain

Council approval for all position salaries and for the creation of any new staff positions.

The result of this combined Executive and Legislative oversight produces a series of checks and balances that can, when fully exercised, assure a high level of scrutiny of City Light's policies, budget, and operating policies and procedures.

Seattle City Council

The Seattle City Council has typically engaged in governance and oversight of City Light through a specific committee. Currently, the three-member Energy and Environmental Policy Committee includes Heidi Wills, chair; Jim Compton, vice-chair; and Margaret Pageler, former chair of the committee, the third standing member. The alternate is Richard Conlin, who served as a member the last two years and who attends in the absence of another member.

In addition to the legislative assistants working directly for individual Councilmembers, the City Council is supported in its decision-making by a 15-member central staff that works for the entire Council. The staff includes attorneys, financial analysts, and policy professionals with expertise in a wide range of issues. In any given year, four to five members of this staff are assigned on occasion to specific projects related to City Light, with a limited number dedicating a significant share of their time to utility issues.

The role of the City Council's central staff is to provide the Council with objective, well-informed policy analysis. Most often the staff's work involves critical analysis of executive proposals, but the team is also involved in developing Council initiatives. Typically, central staff researches an issue, asks questions of executive staff, and summarizes its findings in a memorandum. If legislation is involved, staff then assists the Council in its formal review of the legislation and with the preparation of any amendments.

Executive Management

In the recent past, there have been varying degrees of staffing oversight of City Light at the executive level. A number of budget analysts in the Department of Finance or its equivalent have been primarily responsible for review of the utility's annual budget, rate proposals, and other financial activities. The City's debt manager (in the Department of Finance) has coordinated City Light bond sales and assisted in developing financing tools such as the Revenue Anticipation Notes issued last year.

At times, policy analysts (with varying degrees of skill and experience) have provided the Mayor with a higher level of strategic and analytical review. These analysts have worked for the Mayor, either directly in his office or through a central policy office. Additionally, someone at a senior level (often a Deputy

Mayor) in the Mayor's Office has partial responsibility for coordinating executive oversight of City Light. From administration to administration, the level of direct Mayoral involvement has also varied significantly.

In the current administration, the Superintendent of City Light reports to the Mayor through his chief of departmental operations. This senior executive, who oversees all City departments, has biweekly meetings with the Superintendent to discuss on-going operational issues, proposed legislation, and policy and financial issues of the utility. These regular meetings provide the Mayor's staff with information on current and future issues, as well as an opportunity to discuss the status of the utility's work program. It also provides an opportunity to discuss policy direction and/or operational matters directly with the Superintendent.

The Department of Finance coordinates bond sales with the utility, reviews rate proposals, and provides financial analysis and advice on other financial instruments considered by City Light. A budget analyst is assigned to City Light to provide analysis on City Light issues for the Mayor's Office. Primarily focused on financial and administrative operations, this analyst is responsible for reviewing City Light policy recommendations prior to forwarding them to the Mayor's Office.

Finally, the newly created Office of Policy and Management dedicates part of a position to City Light issues, and provides some additional policy analysis capacity. This new position is an important recognition of the need for more staff, but the current part-time resource is insufficient to achieve the necessary level of oversight.

A City Light Citizen's Rate Advisory Committee is convened when needed to provide advice about key aspects of proposed electric rate actions.

Benefits of the Current Governance

The current governance structure for Seattle City Light offers its share of strengths, including:

- ***The combination of Executive and Legislative oversight increases the likelihood of sound policy decisions.*** More levels of independent review can strengthen the necessary policy development dialogue that must occur to ensure thoughtful, well-informed oversight.
- ***The system of checks and balances minimizes the possibility of City Light becoming a political tool of one branch of government.*** Any effort to use the resources of City Light to advance the political agenda of one elected body can be countered by the other.

- ***Governance of City Light is provided by officials who are accountable to ratepayers through elections.*** If the public or “owners” of the utility are unhappy with its governance, they can institute a change through the ballot box.
- ***Public power is publicly governed.*** Policies are set with the opportunity for full scrutiny and public involvement. Operations of the utility can reflect the broader social and political goals of the community, such as universal access and environmental protection.

Weaknesses of the Current Governance

Seattle City Light has been governed within essentially the same structure (some changes to the City Charter over the years have refined the system) for almost a century. The world of 1910, when the City Lighting Department was created, was a much different world than the one in which we live today. Consequently, some aspects of Seattle’s governance of City Light have hampered the utility’s ability to respond effectively to changes in market and regulatory conditions. These weaknesses include:

- ***The electric utility industry has become far more complex, requiring a much higher level of business sophistication from elected officials.*** For much of the history of City Light, the utility has been able to control its own destiny. It could build dams and sell power to its own customers, however it chose. There appeared to be limitless opportunities to create supply and, at the same time, a limit of demand, thus providing ample opportunity to keep rates low. Likewise, with an abundance of fish, fresh water, and fresh air, environmental impacts were far from most people’s minds.

Obviously, much has changed over time. Risk management stands as an example of this increased complexity. Historically, elected officials were called on to master basic public policy and public finance. Today, a complex, fast-changing energy market also requires the Mayor and City Council to provide policy direction and management oversight for a very complex power portfolio and its attendant risks.

- ***Because of this increased complexity in the industry, elected officials need to commit more time and effort than ever before to govern City Light.*** This can be difficult when these same officials are called upon to legislate regarding other pressing political issues. These issues often have political advocates who are more vocal, drawing a greater level of media coverage, and therefore greater time and attention from elected officials. Despite their long-term impact on the financial well being of the utility, some City Light decisions may be given a relatively

cursory review by a Mayor and City Council members who find themselves occupied with other issues.

- ***Sometimes decisions about utility issues appear to be based on short-term politics rather than on the long-term well being of City Light.*** The Mayor and City Council are re-elected based on their actions of the past four years, but the implications of the City Light decisions they make during their tenure may last for generations. There can be an irresistible temptation to appease short-term interests, such as keeping electric rates low, even at the expense of long-term borrowing costs. Likewise, the seemingly unlimited financial resources of City Light can be an attractive target for funding City expenses unrelated to the utility's core mission.
- ***Elected officials are rarely elected based on their oversight of Seattle City Light, thus no one is held accountable for their performance regarding the utility.*** With a broad agenda of issues to cover, oversight of City Light becomes just one, relatively invisible component of a re-election platform. Absent a ratepayer or other utility advocacy group and the media attention they attract, City Light oversight rarely rises to the level of determining an election's outcome. Elected officials may, therefore, see less political benefit to devoting their limited time and resources to provide effective oversight of City Light.
- ***Lack of guaranteed continuity and institutional memory.*** Every two years, there is an opportunity for changing the elected officials governing City Light. In recent times, we have seen a high level of turnover in Council members and in the Mayor's office. Although this may speak well for our democracy, changes in leadership threaten the stability of City Light, especially at a time when there is such a premium on knowledge and understanding of the electric utility industry.

City Light – A Unique Department

Seattle City Light has a number of characteristics that make it truly unique when compared to other City departments. Effective oversight of City Light must acknowledge these differences.

- ***A pervasive service:*** Although other City departments exist to provide service to all the people of Seattle, it is only the utilities that will actually be called on to do so – to all citizens, all at once, all the time. Police and fire departments have to prepare to provide service in an emergency; utilities create emergencies if their service is not delivered, even for a few hours.
- ***Technically complex:*** There is an exceptional level of technical complexity inherent in providing electricity service to all current and future

residential, commercial, and industrial customers 24 hours a day, 365 days a year. An example of this is a routine task performed by the utility's power dispatchers. The West Coast power grid must maintain a balance between what utilities draw from to meet customer demand and what generators supply back to it. An imbalance for more than a few seconds can bring the grid down, blacking out the entire region. City Light is part of that grid and its dispatchers bear a share of the responsibility for maintaining that balance throughout the West Coast. Second-to-second, they make decisions that have implications far beyond Seattle's borders. The skill needed can only be acquired through years of training and apprenticeship.

- ***Capital-intensive:*** City Light's capital assets total about \$1.2 billion. These include the dams, generation plants, substations, distribution facilities, and a host of supporting facilities and equipment. Maintenance and replacement of these assets requires an annual capital investment of more than \$150 million. Many of the utility's assets can have useful lives in excess of 50 years, with proper care and attention. As the utility's own experience with its low-cost hydroelectric generation plant clearly demonstrates, wise investments can return exceptional value to the community over very long periods of time.
- ***Impact of federal regulations:*** While City Light is run by the City of Seattle, many of its operations are regulated or affected by federal (particularly FERC), as well as state guidelines. The Mayor and City Council have limited authority to direct much of City Light's power generation, transmission, and marketing policies. Because of this level of federal involvement, a greater burden is placed on the City to forge alliances with other jurisdictions to influence the outcome of federal and state legislation and regulation.
- ***Importance of regional relationships:*** Electrons know no borders. The efficient generation and distribution of electricity in Seattle requires a seamless fabric of publicly owned utilities, investor owned utilities, and federally owned transmission systems throughout the West. We purchase and sell power, generate new power, and transmit electricity across many different state and local jurisdictions. Therefore, Seattle cannot afford to make decisions in isolation. The impact of local policy decisions on regional partners must be considered, as must the decisions of regional players be considered as affecting City Light. In no other City department is this level of regional participation so important.
- ***Factors outside the City's control:*** There is nothing the City can do to affect the weather, and rainfall levels play an enormous role in the economic stability of City Light. In particular, the level of snow pack created each winter largely determines the amount of available

hydroelectricity for the year. Market prices also are outside the City's control, dependent as they are on a complex web of factors and players throughout the United States and Canada. While City Light can attempt to predict combinations of factors and the impacts they will have on price and operations, it will always have to react to variances between forecasts and real-time market realities.

- **Commodity trader:** Unique among City departments, City Light has an active commodity trading function that is critical to fulfilling the utility's obligation to meet customer demand for electricity. Because of the complexity of City Light's hydroelectric system, even experienced energy traders require months of training on the system before they are qualified to trade for the utility. Every day, they make decisions involving millions of dollars; during the recent energy crisis, the decisions involved tens of millions of dollars.

Commodity risk management requires a level of statistical and financial sophistication usually found only in those with an advanced degree in economics, finance, or physics. The electricity market is widely accepted as the most challenging arena in which to operate, and managing risk for a hydroelectric-based utility the most challenging within that arena. This work requires a level of knowledge and sophistication virtually unlike any other performed by municipal employees.

Attributes of Successful Governance

As the "shareholders" of Seattle City Light, the public expects a high standard of oversight of its assets, and elects a Mayor and City Councilmembers to exercise these standards regularly and rigorously. The following list includes those characteristics the Mayor's Committee feels are critical to the effective, responsible oversight of City Light. The inclusion of this list is intended to be a measure for whatever changes are made in the governance structure of City Light.

- **Open and public decision-making.** Important policies should be considered and debated in public, with meaningful opportunities for the public to participate and to influence decisions. Advance notice of discussions, information on the Internet, inclusion of notices within electricity bills, televised City Council proceedings, and public hearings are all effective tools to encourage public participation. Convenient, straightforward avenues for accessing information about adopted policies should be available to every citizen. The policies should be clearly articulated and easily located.
- **Concurring resolutions.** All policies governing City Light should be negotiated and adopted as City Council resolutions, with the Mayor

concurring. These policies should address finances and rate structures, power supply and conservation, risk management, and other policy areas selected by the Mayor and City Council. As policies are adopted, the Mayor and City Council should negotiate a work program for implementing them. These policies should be posted for public review on the City of Seattle's website.

- **Clarity of strategic direction.** On a regular basis, the City Council, Executive, and City Light management should attempt to articulate and agree on a clear, written statement of strategic goals and objectives, against which the operations of City Light can be regularly measured. As an example, these might include measures for:
 - ❑ Risk management
 - ❑ Financial performance
 - ❑ System reliability
 - ❑ Customer satisfaction
 - ❑ Employee and management development
 - ❑ Environmental protection
 - ❑ Conservation and resource development

The choice of measures should be spurred by a thoughtful, robust debate on the utility's strategic direction, and that the final statement be one all parties are working to achieve together.

- **Clear and realistic work programs.** Once City Light's strategic direction is established by the Mayor and City Council, City Light management should be responsible for creating the work programs needed to meet the strategic goals and objectives. There should be regular reporting on work program progress, and evaluation of the Superintendent and the utility should be based upon their success in meeting these goals and objectives.
- **Flexibility.** Recognizing the importance of a strategic direction for City Light, acknowledgement of the volatile nature of the electric power industry is also important. Even the best forecasts could not have predicted the wild price spikes of recent years or the severe drought that occurred simultaneously. City Light must be prepared to respond quickly to market changes.
- **Business and utility sophistication.** Elected officials are usually drawn to the public policy side of City governance, but City Light also requires a level of business and utility sophistication in order to make the best decisions. If those who oversee the utility do not already possess significant experience in the electricity utility industry, they must be prepared to dedicate the time required to fully educate themselves.

Additionally, staff in the Legislative and Executive departments should have business and utility expertise, and they should focus exclusively on City Light to help brief and frame decisions for the elected officials.

- ***Advocacy for the long-term health of the utility.*** Somewhere within government there needs to be a strong and respected voice devoted to Seattle City Light's institutional interests and assets, including financial resources, and protecting them from competing demands. This voice needs to be ongoing, not just periodic. Ad hoc and intermittent citizen advisory committees do not provide the continuity or the breadth of knowledge to serve this advocacy purpose well.
- ***Advocacy for ratepayers.*** An avenue for ratepayer involvement in electric rate decisions must be provided. Such avenue should complement existing structures for citizen involvement (such as an advisory board or governing board). For example, a ratepayer committee may be most effective if it is newly assembled for each rate case and equitably represents all affected customers.
- ***Continuity of governance.*** Because elected officials serve at the pleasure of the voters, changes in the leadership of City Light oversight is possible every two to four years. Newly elected officials, especially a new Mayor or a City Council member serving on the committee overseeing City Light, must commit significant time early in their terms to learning the electric utility industry. City Light must commit to instituting a comprehensive orientation program. In the process of re-educating a new cast of leaders every two to four years, the utility may lose its window of opportunity to respond to critical issues. Some structure not subject to elections needs to provide continuity of knowledge and governance for the utility.
- ***Regional Participation.*** Elected officials must actively participate in regional and national organizations to influence the federal and state regulatory environment, as well as to create business alliances. This participation must ensure effective representation of City Light's interests, but also the regional interests and institutions of the Pacific Northwest, which are essential partners and neighbors of our municipal utility.

Committee's Recommended Changes:

The Mayor's Committee has prepared a number of recommendations that build on the strength of the current system of City Light governance while helping to mitigate its weaknesses. Additional recommendations help assure a sufficient review of City Light policies is undertaken by elected officials prior to their adoption, and others provide City Light with the tools needed to manage the utility effectively.

1. *The Mayor's Committee unanimously agrees that the complex and dynamic nature of the electric utility industry requires the addition of a strong, independent board, exclusively focused on City Light policy issues.*

Such a board is critical to providing an independent voice regarding utility oversight, helping to insulate City Light from the short-term political pressures that can occupy elected officials, and to maintain the utility's focus on its core mission. Additionally, this board can bring a level of expertise and in-depth consideration of policy issues that elected officials may not have the time or background to provide. The board should be comprised of highly qualified individuals, from a diverse range of backgrounds, each of them striving to provide the best-informed, objective counsel to the Mayor, City Council, and City Light management.

We observed that under the current governance system there is a potential conflict between preserving the long-term financial health of City Light and responding to more immediate public policy and political pressures. This imbalance is often caused by the higher political profile of near-term public policy decisions, such as rates and environmental impacts. For instance, plenty of loud voices urge low electric rates, but many fewer thoughtful voices warn of the risks low rates might present in terms of long-term financial stability, including the levels of debt incurred. An independent board would help bring balance to this equation by creating a respected, knowledgeable, and independent body to provide strategic advice, even advocacy, on key policies.

2. *While the Mayor's Committee unanimously recommends the creation of an independent board, we are evenly divided on the question of whether this board should possess governing authority or whether it should be advisory only.*

Half of the Mayor's Committee (Craig Gannett, Randy Revelle, and Sam Sperry) believes an **advisory** board will address most of the shortcomings in the present governance system. They recommend an advisory board rather than a governing board because they believe the Mayor and City Council should retain accountability for governing City Light. An advisory board preserves the direct linkage between Seattle's elected officials and the voters who, in effect, are the utility's "stockholders."

The other half of the Mayor's Committee (Sharon Nelson, Richard Sonstelie, and Keith Warner) is not confident an advisory board will provide the required level of expertise, nor sufficient insulation of utility governance from short-term political pressures. They fear that an advisory board with no governing authority will be marginalized and eventually ignored, and will cease to attract the caliber of members required. Fundamentally, these three committee members believe the

magnitude of changes that have taken place and are likely to continue in the electric utility industry mandate a more systemic change to City Light governance.

Nelson, Sonstelie, and Warner think an independent ***governing*** board should be established, possessing the powers that are usually exercised by corporate boards such as setting rates, issuing debt, and approving budgets. The board should also have the authority to hire and fire the Superintendent of City Light. Members of this board would be appointed by the Mayor and confirmed by the City Council. These three committee members argue that such a governance structure would better position City Light for an energy future that will require focused, flexible, and quick decision making.

Gannett, Revelle, and Sperry disagree with this recommendation. They fear the addition of an entity outside the current City structure would diminish accountability for City Light governance. As officials elected by Seattle voters and ratepayers, the Mayor and City Council should be responsible to them for the governance of City Light. These three committee members cite examples in Washington state government where authority has been dispersed to independently elected offices such as those of the Commissioner of Public Lands and Superintendent of Public Instruction, limiting the Governor's ability to provide effective leadership and oversight of those critical state functions. Establishing a new governing board might be an appealing departure from tradition in response to today's energy environment, but once established, it could prove to be an impediment rather than an aid to more effective governance. They fear that a new governing board could lose touch with the public purposes and values elected officials are expected to nurture.

Establishment of an independent governing board with the responsibilities proposed above would require changes to the Seattle City Charter and to state law, which provides that the City Council alone can issue debt and set rates for City Light. The entire Mayor's Committee is mindful of the difficulty of amending the City Charter and convincing the Washington State Legislature to change state law. Furthermore, even if the Legislature could be convinced to do so, the committee recognizes that the timeline would be lengthy.

- 3. Given the fast-paced changes in the electric utility industry, the Mayor's Committee believes the creation of an independent advisory board should be pursued promptly. Therefore, the committee is united in calling for the early establishment of a City Light Advisory Board, with the recommended requirement that the Mayor and City Council assess the efficacy of the board within three to five years of creating it.***

In establishing the advisory board, the Mayor's Committee unanimously recommends the following:

- A City Light Advisory Board should be established by ordinance.
- The board should be composed of five to seven members.
- All members should be appointed by the Mayor, subject to confirmation by a majority vote of the City Council.
- Advisory board members should have demonstrated expertise and experience in one or more of the following areas: business, finances, energy conservation, environmental protection, energy law, utility operations and power/risk management. The composition of the board is intended to provide expert, diverse perspectives and not be representational.
- Members should be appointed for three year, staggered terms.
- Members may be reappointed for a second term.
- The advisory board should advise the Mayor, the City Council, and the City Light Superintendent on policies and operations related to the utility's finances, power supply, risk management and energy conservation.
- The Mayor and the City Council should provide the staff support needed to carry out the responsibilities of the advisory board. The City Attorney should provide necessary legal advice.

The staggered, three-year terms would help to bring a level of continuity to City Light governance, since each board term would span an election cycle. It is critical the board be adequately staffed.

To increase the likelihood the advisory board's advice will be given due consideration, the ordinance establishing this board should include the following language:

- "The Mayor, Seattle City Council, and Superintendent shall give every serious consideration to all recommendations of the advisory board."
- "Should the Mayor and/or City Council determine it is necessary to reject or modify any written recommendation of the advisory board, the Mayor and/or the Chair of the Council's Energy and Environmental Policy Committee, or successor committee, shall, within thirty days of rejecting or modifying such written recommendation, explain in writing why the advisory board's recommendation is being rejected or modified."

The board's recommendations and the Mayor and/or City Council's reasons for rejecting them should be publicly available, including posting on the City's website.

Once the board is formed, it should work with the Mayor and City Council to reassess the role of the Rate Advisory Committee. The Mayor's Committee believes there will be an important need for customer review of rate

recommendations that can complement, but not be replaced, by the work of the advisory board.

The other recommendations of the Mayor's Committee, which follow in this report, should also be put in place promptly. We all agree the success of City Light cannot be placed on the shoulders of an advisory board alone. The Mayor and City Council should commit to redirecting resources to ensure an upgraded oversight of City Light and should implement the other recommendations contained in this report.

4. If within three to five years the Mayor and City Council cannot demonstrate the efficacy of the advisory board, the Mayor's Committee unanimously recommends the Mayor and City Council attempt to change the City Charter and state law to allow for the establishment of an independent structure to govern City Light.

Assessment of the advisory board's efficacy should take into account:

- The political judgments of the Mayor and City Council;
- Public comment, including the perspectives of ratepayers; and
- The perspectives of advisory board members who have been serving during that initial period.

Among other models to be researched at that point, the committee suggests looking closely at the structure of an independent city agency, such as the one governing the Jacksonville Energy Authority in Jacksonville, Florida; or a city-owned public corporation such as the one used in Toronto, Canada.

5. The Mayor's Committee recommends providing more staff resources in the Executive and City Council offices. Specifically, a senior-level staff person should be added to the Mayor's Office or the Office of Policy and Management. Additional staff resources in the Budget office and City Council office should focus on policy development and oversight, rather than daily operational issues of City Light.

To make the best policy decisions, the Mayor and City Council need access to thorough, well-developed proposals, analyzed independently from Seattle City Light. Experienced analysts need to be knowledgeable enough to ask tough questions of the utility management and staff, be able to challenge assumptions, and frame the implications of policy decisions. This analytical staff capacity needs to be increased in both the Executive and Legislative offices to facilitate policy review in both branches.

This change should strengthen the necessary policy development dialogue that must occur among the Executive, the City Council, and City Light staff to ensure thoughtful, well-informed oversight actually occurs. The committee specifically

recommends a senior-level staff person, experienced in the public electric power industry, be added to the Mayor's executive staff. This person should focus exclusively on City Light's top priority issues of intermediate and long-term importance, not daily operational matters.

Staff dedicated to the oversight of City Light has ebbed and flowed too often at the mercy of political tides and near-term budget concerns. Now more than any time in City Light's past, continuity, stability, and well-informed oversight are critical to its success.

The City needs to prioritize its resources to provide this greater level of dedicated staff. If an advisory or governing board is formed, it will require staff support as well. To the extent feasible, the additional staff should be provided within existing resources. If necessary, they should be funded with additional resources.

6. The Mayor and City Councilmembers should commit a greater amount of time and effort to governance and oversight of Seattle City Light.

In recent years, the amount of attention paid to City Light by Mayors and City Councilmembers has varied significantly. These elected officials must commit the time and effort to examine and understand highly complex and technical utility issues. Indeed, if they cannot or will not, then a separate utility governing board may ultimately be the only answer. There is an undeniable correlation between time and effort spent and the quality of governance and oversight. In the absence of informed direction from elected officials, the role of guiding the utility necessarily falls to non-elected management staff. Such an outcome does not keep faith with the voters.

7. In addition to committing the time and effort to understand the complex and technical issues influencing Seattle City Light, the Mayor in particular and City Councilmembers as appropriate must lend their stature to regional partnerships and other efforts to influence the direction of state, regional, and federal decisions that affect public power utilities directly and indirectly.

The job of advocating for City Light's interests in the face of federal and state legislative and regulatory changes has fallen recently to utility management staff. Instead, the Mayor of Seattle, as the most visible and influential representative of the City, is best positioned to advocate for the utility in certain federal and regional venues. As the recent past shows, we have much to gain and even more to lose in regulatory restructuring. Heading off ill-advised legislative or regulatory proposals could be one of the most important actions taken by a Mayor to protect City Light.

8. *The Mayor and City Councilmembers must carefully examine the issues and challenges of the power/risk management functions, and then establish clear policies to guide them.*

One of Seattle City Light's fundamental responsibilities is to provide sufficient energy resources to meet the demands of its customers at every moment. This is not a new obligation. The utility has performed this function since its inception. Recent and pending changes in the regional and national electric utility industry are increasing the complexity of this function and increasing the financial consequences.

Power/risk management has always had to deal with a great deal of uncertainty:

- Weather determines the amount of water available at any given time for generating electricity and can have a strong effect on electricity consumption; and
- Wholesale market prices are volatile and beyond the utility's control.

Over the last few years, the West Coast wholesale power market has become increasingly complex and volatile. To carry out City Light's fundamental power supply responsibilities, the utility is now effectively engaged in commodity trading, with all of its attendant risks and challenges.

The fundamental structure of the wholesale power markets will probably continue to evolve, perhaps dramatically, over the next few years. Within this context, the Mayor's Committee recognizes the special challenges power/risk management present for City Light and the elected officials responsible for governing the utility. For example, weather contingencies will always present real time challenges to reasonable forecasting efforts. Effective market participation will require decision making at a pace unusual for the traditional local government process.

Because the financial risks associated with these activities are so large, City Light must have an effective framework for managing these risks, and the City's elected officials must provide the utility with strong policy direction for these functions.

Based on our review of these issues, the Mayor's Committee does not feel there has been a sufficient focus on assessing the utility's approach to power/risk management or the elected officials' oversight of these management functions. Current procedures have not been thoroughly reviewed for their effectiveness, and the existing policy direction is fragmented and incomplete. An affirmative review of existing management structures, procedures, and governing policies is clearly necessary with respect to the power/risk management functions.

City Light is in the best position to frame the range of management alternatives, including pooled efforts within the region, and to outline the type of policy guidelines that will be needed to guide the selected management model. To develop an appropriate consensus, however, a final assessment of these alternatives should be performed collaboratively by the Mayor, City Council, and appropriate City Light officials. This process will best be facilitated by an outside contractor with strong credentials in the municipal electricity risk management field. Regardless of the direction the City selects for future power/risk management oversight, a well-informed and comprehensive policy direction is an essential element of future success.

9. Mayoral and City Council policy staff should become more directly involved in City Light's power/risk management decision process by participating regularly in City Light's weekly Risk Management Committee meetings.

In order to ensure the Mayor and City Council develop and maintain a well-informed grounding in risk management issues, the Mayor's Committee believes Executive and City Council policy staff should become more directly exposed to City Light's power/risk management decision process. Knowledgeable staff committed to City Light affairs can assist elected officials in staying on top of emerging utility issues and concerns.

Regular participation in Risk Management Committee meetings would raise the overall knowledge level of this complex business activity, better inform policy decisions, and provide more timely awareness of emerging challenges. The Executive and Legislative staff will need to respect the potential confidentiality of market sensitive information and to honor the decision-making authority of City Light executive personnel. With respect to the latter, it should also be made clear at the outset that participation in such meetings will not constitute an endorsement by either the City Council or the Mayor of specific utility management decisions.

10. City Light requires the flexibility to operate outside some City systems, particularly those governing salaries.

City Light's power management staff is charged with making decisions that require an exceptional level of knowledge, extensive experience, and business sophistication. The choices they make can earn or cost the utility hundreds of millions of dollars each year. There is no parallel to this function elsewhere in City government.

In recruiting for qualified risk/power management staff, City Light competes against the private sector, not against other City departments or other public agencies. Thus, the power management salaries need to compete with those of the private sector. Mayor's Committee members noted that on a dollar-for-dollar

basis, failure to pay sufficient salaries could result in a shift of a million dollars to or away from the utility based on the experience of the person making a transaction. Not to raise certain of these salaries could well prove to be a policy that is penny wise and pound foolish.

Many other utility jobs besides power marketing require a high level of technical expertise. City Light competes for the services of these skilled engineers and professionals as well. Many of City Light's professional staff appear to be underpaid in comparison to their private sector counterparts. The benefits of working for the City can help to compensate, but these intangible advantages cannot be relied upon to make up the difference. The utility needs the flexibility to compete for top-flight talent in the marketplace by setting competitive salary scales.

Conclusion

To develop our recommendations, we received very informative and candid presentations from a former Seattle City Light Superintendent, the current City Council Energy and Environment Committee members, the Power Committee Chair of the Northwest Power Planning Council, and utility management staff in Seattle and Tacoma. We read and considered volumes of information. We plumbed our own extensive experience working on electric utility issues in both the public and the private sectors.

Repeatedly, we heard there are no panaceas, no perfect, one-size-fits-all governance model for an electric utility in these times. After four months of study, we would share this view. Each existing model governing public utilities throughout the country offers the ability to succeed or fail based upon the quality, experience and dedication of the individuals who make the decisions and who do the work. Thus, our report makes recommendations for enhancing the knowledge of those individuals, including elected officials and utility staff within the system.

The unique responsibilities of Seattle City Light to the economic development of the region require a unique brand of governance and oversight by elected officials. With regulatory and market changes happening so rapidly, each day can bring difficult new challenges, with implications for the long-term well being of City Light and the community it serves. We respectfully urge the Mayor and City Council to consider our recommendations seriously, and to begin implementing them promptly.

Respectfully submitted:

Mayor's City Light Review Committee

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